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No. 97-1287

In The

Supreme Court of the United States

OCTOBER TERM, 1997

HUGHES AIRCRAFT COMPANY, *et al.*

Petitioners,

v.

STANLEY I. JACOBSON, *et al.*

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

MOTION OF THE ERISA INDUSTRY COMMITTEE FOR LEAVE TO FILE *AMICUS CURIAE* BRIEF AND BRIEF *AMICUS CURIAE* IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

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The ERISA Industry Committee ("ERIC") hereby moves, pursuant to Rule 37.2.(b), for leave to file the attached brief *amicus curiae* in support of the Petition for Writ of Certiorari. Petitioners have consented to the filing of the attached brief. A letter evidencing petitioners' consent has been lodged with the Clerk. Respondents, however, have declined to consent.

ERIC is a nonprofit organization representing over 130 major employers. It frequently participates as *amicus curiae*

in cases with the potential for far-reaching effects on employee benefit plan design or administration.[1]

Virtually all of ERIC's members maintain one or more defined-benefit pension plans governed by the Employee Retirement Income Security Act of 1974 ("ERISA"), 29 U.S.C. § 1001 *et seq.* A substantial number of those plans, including some of the very largest pension plans in the United States, accept or require employee contributions or have done so in the past. The opinion of the court of appeals has potential far-reaching effects for virtually all defined-benefit pension plans that have or have had an employee contribution feature, and quite possibly for many other employee benefit plans with contributory features.

The court of appeals held that plan amendments that add an early retirement feature and that create a new benefit formula for plan participants who do not contribute to the plan are subject to attack as breaches of fiduciary duties owed to other plan participants. This conclusion is of great interest and concern to the members of ERIC and numerous other employers who maintain defined-benefit and other plans.

The conclusion by the court of appeals that a plan amendment that adds a new benefit formula for some participants can be found to constitute a "constructive termination" of the plan for purposes of ERISA also is of great concern to ERIC and its members. Since plan amendments of this sort are quite common, and since the termination of a plan has enormous consequences for both

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[1] For example, ERIC participated as an *amicus* before this Court in *Lockheed Corp. v. Spink*, 116 S. Ct. 1783 (1996), *rev'g* 60 F.3d 616 (9th Cir. 1995). *See also Firestone Tire & Rubber Co. v. Bruch*, 489 U.S. 101 (1989); *Metropolitan Life Ins. Co. v. Taylor*, 481 U.S. 58 (1987).

employers and employees, the members of ERIC have a vital interest in the appropriate resolution of this issue.

Because it represents numerous employers, ERIC is in a position to provide a broader perspective than any party to this litigation can provide. Because the issues posed by the court of appeals' decision are so far-reaching and significant, the Court may benefit from having that broader perspective before it when it considers whether to grant the Petition for Writ of Certiorari. Accordingly, ERIC respectfully requests that its motion for leave to file a brief *amicus curiae* in support of that petition be granted.

Respectfully submitted,

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BRIEF OF THE ERISA INDUSTRY COMMITTEE AS *AMICUS CURIAE* IN SUPPORT OF THE PETITION FOR WRIT OF CERTIORARI

The ERISA Industry Committee ("ERIC") submits this brief *amicus curiae* in support of the Petition for Writ of Certiorari.

INTEREST OF *AMICUS CURIAE*

ERIC's interest is set forth in the foregoing Motion for Leave to File.

SUMMARY OF ARGUMENT

The Court should grant the petition for the following reasons:

The conflict on the breach of fiduciary duties issue between the court of appeals' decision and this Court's decision in *Lockheed Corp. v. Spink*, 116 S. Ct. 1783 (1996), and between the court of appeals' decision and the decisions of other circuits, is particularly acute. As matters now stand, a plan amendment that would be held to be clearly lawful in several circuits could be held unlawful in the Ninth Circuit, so that the legality of a plan amendment could turn on the fortuitous circumstance of which of many possible jurisdictions the litigation is filed in. The uncertainty engendered by the court of appeals' decision thus creates a substantial deterrent to the adoption of plan amendments offering new or enhanced benefits for participants.

The holding of the court of appeals that participants in a contributory defined-benefit plan have a broad beneficial ownership interest in the plan's so-called "surplus" is contrary to the holdings of at least three other circuits, is based on an erroneous extrapolation from two narrowly-focused statutory provisions, and is likely to have (until reversed) a serious unsettling effect on the development and administration of employee benefit plans.

The holding by the court of appeals that the question whether a plan has been terminated, constructively or otherwise, presents an issue of fact is inconsistent with the holdings of other circuit courts to the effect that the Employee Retirement Income Security Act of 1974 ("ERISA"), 29 U.S.C. § 1001 *et seq.* provides the exclusive means of terminating a defined-benefit plan.

Pursuant to Supreme Court Rule 37.6, ERIC states that this brief was not prepared, written, funded or produced by any person or entity other than ERIC or its counsel.

ARGUMENT

I. UNTIL IT IS REVERSED OR OVERRULED, THE DECISION BELOW ON THE BREACH OF FIDUCIARY DUTIES ISSUE WILL BE A SOURCE OF CONSIDERABLE UNCERTAINTY AMONG SPONSORS OF ERISA PLANS AND A SUBSTANTIAL DETERRENT TO THE ADOPTION OF PLAN AMENDMENTS OFFERING NEW OR ENHANCED BENEFITS TO PARTICIPANTS.

Less than four years ago, a unanimous panel of the Seventh Circuit held that retiree-participants in a contributory defined-benefit pension plan had no claim for breach of fiduciary duty under ERISA with respect to a plan amendment that eliminated the plan's "surplus" by greatly increasing the benefit obligations to existing employees (but not to retirees) in the event of a hostile takeover. *Johnson v. Georgia-Pacific Corp.*, 19 F.3d 1184, 1188-90 (7th Cir. 1994) (Easterbrook, J).[1]

Less than two years ago, this Court held, *inter alia*, that plan amendments creating new benefit opportunities for employees who, among other things, are willing to release all their existing legal claims against the employer are not "prohibited transaction[s]" and do not implicate any of the fiduciary duties imposed by ERISA. *Lockheed Corp. v. Spink*, 116 S. Ct. 1783, 1790, 1792 (1996).

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[1] Other circuits also have concluded that employer amendments to ERISA plans do not implicate ERISA's fiduciary duties. *See, e.g., Malia v. General Elec. Co.*, 23 F.3d 828, 833 (3d Cir.), *cert. denied*, 513 U.S. 956 (1994); *Musto v. American Gen. Corp.*, 861 F.2d 897, 912 (6th Cir. 1988), *cert. denied*, 490 U.S. 1020 (1989); *Salazar v. Sandia Corp.*, 656 F.2d 578, 580 (10th Cir. 1981).

Now a two-member panel majority in the Ninth Circuit has rendered perilous any reliance on *Johnson* and its progeny,[2] and any reliance on *Lockheed* if the plan has accepted employee contributions. The panel majority's decision squarely conflicts with *Johnson* and its progeny, and purports to distinguish *Lockheed* in ways that are quite at odds with the language and rationale of this Court.[3]

Today, employers that have added early retirement and other benefit improvements to their contributory plans in recent years, possibly in reliance on *Lockheed*, *Johnson*, and similar decisions, face the prospect of defending costly litigation predicated on the court of appeals' decision. Literally thousands of plans with cumulatively millions of

[2] The panel majority attempted to reconcile its decision with *Johnson* on the ground that *Johnson* involved only an increase in benefits for active employees who already were plan participants, while the plaintiffs in this case alleged a transfer of plan assets for the benefit of yet-to-be hired employees. *See* Pet'r App. 17a. However, the panel majority held that petitioners may be liable for a breach of fiduciary duty because they used plan assets to provide eligible employees with a new early retirement opportunity. *Id.* at 25a. Since only current active employees can possibly qualify for early retirement benefits, the court of appeals' effort to distinguish *Johnson* is baseless.

[3] The Ninth Circuit in *Lockheed* held that the addition of an early retirement feature to a plan, at least where participation in that benefit was conditioned on the employee executing a release of various legal claims against the company, constituted an impermissible use of plan assets for the benefit of the employer and thus a breach of the employer's fiduciary duty. *Spink v. Lockheed Corp.*, 60 F.3d 616, 622-24 (9th Cir. 1995). This Court reversed, not as the Ninth Circuit now contends because Lockheed employees made no contributions to the plan, but because the addition of new benefits to a pension plan is a settlor function that does not implicate ERISA's fiduciary duties. *Lockheed Corp. v. Spink*, 116 S. Ct. 1783, 1790 (1996). That rationale does not support the distinction the Ninth Circuit now seeks to draw between contributory and noncontributory plans.

participants and combined assets of billions of dollars are put at risk by the court of appeals' decision.[4] Moreover, because ERISA contains very permissive jurisdiction and venue provisions, *see* ERISA Section 502(e)(2), 29 U.S.C. § 1132(e)(2), it is often difficult if not impossible to predict the circuit in which litigation will occur. For employers that are contemplating adding new benefits to their contributory plans and that could be sued in the Ninth Circuit, as would be true for many larger employers, the prudent course may be to defer adoption of any improvements in plan benefits until the uncertainty caused by the decision below is clarified. While such a wait-and-see approach might be a sound business decision, it is contrary to one of the primary purposes of ERISA: the creation of a uniform body of law that encourages employers to adopt and upgrade employee benefits. *See, e.g.*, *Fort Halifax Packing Co. v. Coyne*, 482 U.S. 1, 8-11 (1987). Thus, prompt review and resolution of the conflict by this Court is highly desirable from the standpoint of millions of employees throughout the country.

[4] In 1993, the latest year for which full data have been published, there were 83,596 single-employer defined-benefit plans in the United States, of which 59,372 reported complete actuarial data. U.S. Dep't of Labor, *Funding Status of Defined Benefit Plans*, Private Pension Plan Bulletin Number 6 at 63-64 (Winter 1997). Among those reporting complete actuarial data, 47,023 were "fully funded" plans, with total assets of $827 billion, with "net excess assets" — or "surplus" — of nearly $235 billion and with nearly 26 million participants. *Id.* While it is probable that substantially less than half of these plans accept or once accepted employee contributions, clearly the court of appeals' opinion has potentially very serious far-reaching effects.

II. THE HOLDING OF THE COURT OF APPEALS THAT PARTICIPANTS IN A CONTRIBUTORY DEFINED-BENEFIT PLAN HAVE A BROAD BENEFICIAL OWNERSHIP INTEREST IN THE PLAN'S SO-CALLED "SURPLUS" IS CONTRARY TO THE HOLDINGS OF AT LEAST THREE OTHER CIRCUITS AND IS BASED ON AN ERRONEOUS EXTRAPOLATION FROM TWO NARROWLY-FOCUSED STATUTORY PROVISIONS.

In rejecting the conclusions of at least three other circuit courts,[5] the panel majority reasoned that the so-called "surplus" in a defined-benefit plan that is attributable to employee contributions is a distinct asset in which plan participants enjoy something akin to an ownership interest. "By statutory definition," the panel majority concluded, "employees are vested in their own contributions and the income generated therefrom." Pet'r App. 21a.

This is a serious misapprehension predicated on a misreading of the statute. The essential difference between defined-contribution plans, such as the popular 401(k) plans offered by many private employers, and defined-benefit plans, such as the pension plan at issue here, is that in the former case all the risks and rewards of the investment of the funds fall on the employee-participant. In defined-benefit plans, these roles are reversed. If the investments go sour, the employer must contribute whatever is required to deliver the promised benefit to the employee at retirement. Conversely,

[5] *See Johnson v. Georgia-Pacific Corp.*, 19 F.3d 1184, 1189-90 (7th Cir. 1994); *Brillinger v. General Elec. Co.*, 130 F.3d 61, 64 (2d Cir. 1997); *Malia v. General Elec. Co.*, 23 F.3d 828, 831-33 (3d Cir.), *cert. denied*, 513 U.S. 956 (1994).

a successful investment strategy might lighten and even eliminate for varying periods of time the need for employer contributions. As Judge Easterbrook explained in *Johnson*:

> . . . the retirees do not own the assets of a defined-benefit pension plan. Their contributions purchased not a pool of assets (as would be the case with a defined-contribution plan) but a promise of benefits. 29 U.S.C. § 1002(34). Employees who contribute to a defined-benefit plan are in this respect like persons who purchase annuity contracts from insurance companies. They obtain a guaranteed stream of payments; the insurer (or, with pension plans, the employer) bears the investment risk.

19 F.3d at 1186.

Thus, when a retiree receiving benefits under a defined-benefit plan dies, the retiree's estate receives nothing from the plan, unless the plan itself promises a death benefit. This result cannot be reconciled with the court of appeals' notion of a "vested interest" in all the earnings generated within a defined-benefit plan from an employee's contributions.

The court of appeals' conception of "plan surplus" is irreconcilably in conflict with the view of other circuit courts. Again, *Johnson* is instructive:

> . . . the "surplus" of a defined-benefit plan is . . . not a pile of assets stacked in the corner. It is instead an accounting construct. The plan determines the value of its assets — stocks, bonds, real property, cash, and so on. It also estimates the cost of fulfilling all of the promises to pay vested benefits. The former computation yields the asset side of the balance sheet, the latter computation the liability side. The difference between these is the "surplus" or "deficit" (depending on whether

> the number is positive or negative), which appears on the debit side of the balance sheet to make the two columns tally. Section 1002(21)(A)(i), in conjunction with §§ 1104 and 1106, requires trustees and other persons to deal with the assets of the plan in circumspect and prudent ways. It has nothing at all to say about the debit column on the balance sheet . . ..

Id. at 1189.[6]

The Ninth Circuit's contrary conclusion rests on two narrow statutory provisions that do not alter the general rule that participants in defined-benefit plans have no protected interest in plan assets beyond the right to receive payment of their vested benefits.

The first of these exceptions is the minimum vesting or nonforfeiture provisions of ERISA Sections 203-04, 29 U.S.C. §§ 1053-54 (1994). Far from giving participants a vested interest in all of the earnings attributable to their contributions, these provisions provide only for nonforfeitability of the benefits derived from the contributions themselves plus specified levels of imputed annual interest on employee contributions. *See* 29 U.S.C. § 1054(c)(2)(B)-(C)(1994). The amount of interest imputed to the contributions is fixed by law, and is wholly unrelated to the successes or the failures of the plan's investment strategies. Thus, the minimum vesting requirements do not create a vested interest in the earnings attributable to employee contributions, but merely result in an increase in accrued plan

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[6] Among other variables driving plan "surplus" is the accuracy of the actuarial projections. If plan assets appreciate more rapidly than the actuary predicted, "surplus" grows; if assets grow less quickly or shrink more rapidly than predicted, "surplus" declines.

liabilities — what the *Johnson* court refers to as "the debit column on the balance sheet" — and a corresponding *reduction* in plan "surplus."

The court of appeals also relied on ERISA Section 4044(d)(3)(A), 29 U.S.C. § 1344(d)(3)(A)(1994), which provides that, upon plan termination, if there are assets that are attributable to employee contributions remaining after satisfaction of all plan liabilities, those assets shall be "equitably distributed" to the contributing participants or their beneficiaries.

This highly contingent remainder interest was bootstrapped by the panel majority into a general ownership or beneficial interest in "surplus" no matter whether any termination of the plan has occurred or is contemplated. *See* Pet'r App. 9a. However, plan "surplus" may shrink to as little as zero or become a deficit for any number of reasons, including an unexpected increase in early retirements, retirees living longer than the actuaries predicted, interest rate fluctuations, and stock market corrections. When these events occur, as the court of appeals conceded, the employer has no obligation to make contributions in order to perpetuate the plan's "surplus." *Id.* at 6a (citing *Fetcher v. HMW Indus., Inc.*, 879 F.2d 1111, 1113 (3d Cir. 1989)). In short, participants in a defined-benefit plan have no right under ERISA to insist on perpetuation of a "surplus," even when their contributions account in some measure for that "surplus." That being so, reducing "surplus" by means of plan amendments that provide additional benefits, whether to existing or new participants, or that reduce employee funding obligations, cannot violate ERISA.

Many retirees would no doubt like to have plan "surplus" perpetuated, whether attributable to employee or employer contributions, as that would give them an extra margin of

protection against the possibility of the employer becoming unable to fund the plan. Many other retirees, however, might favor amending the plan to increase payments to retirees, thereby reducing "surplus." But many active employees would no doubt regard a new benefit, such as a special early retirement "window," as a better use of plan assets. Employers would prefer the freedom to add new benefits or to increase existing benefits in whatever manner best serves the employer's interests. An employer might be inclined, for example, to eliminate required contributions by employees if the employer thought that such a step would make the company a more attractive place to work in the eyes of prospective new employees.

As *Lockheed* teaches, on these issues Congress concluded that employers acting in their capacities as plan settlors, not as fiduciaries, can make the decision. And, as an *en banc* Ninth Circuit decision in another case points out, resolution of conflicting policies and interests is

> best left to Congress — particularly when the conflicting concerns and interests arise in an area of the law Congress has chosen to regulate with painstaking detail. *See Nachman Corp. v. Pension Benefit Guaranty Corp.*, 446 U.S. 359, 361, 100 S. Ct. 1723, 1726, 64 L. Ed. 2d 354 (1980) (ERISA is a "comprehensive and reticulated statute").

Hughes Salaried Retirees Action Comm. v. Administrator of Hughes Non-Bargaining Retirement Plan, 72 F.3d 686, 695 (9th Cir. 1995), *cert. denied*, 116 S. Ct. 1676 (1996). Because the opinion of the court of appeals ignored this admonition, and created duties and obligations that are not found in ERISA, *certiorari* should be granted.

III. THE HOLDING OF THE COURT OF APPEALS, THAT PLANS MAY BE DEEMED TO BE TERMINATED WHENEVER A DISTRICT COURT CONCLUDES AS A MATTER OF FACT, BASED ON COMMON LAW TRUST CONCEPTS, THAT TERMINATION HAS OCCURRED, IS ALSO INCONSISTENT WITH THE RULINGS OF OTHER CIRCUIT COURTS AND THREATENS SERIOUSLY TO DISRUPT THE MANAGEMENT OF NUMEROUS PENSION PLANS.

The court of appeals held that the district court could conclude as a matter of fact, based on the common law of trusts, that Hughes' amendments to the plan had caused a "termination" of the plan. *See* Pet'r App. 10a-12a, 22a-23a. This holding is contrary to the law of the Third, Fourth, and Fifth Circuits, where the concept that pension plans can be terminated outside ERISA's statutory framework has been squarely rejected. *See American Flint Glass Workers Union v. Beaumont Glass Co.*, 62 F.3d 574, 579 (3d Cir. 1995); *Phillips v. Bebber*, 914 F.2d 31, 34 (4th Cir. 1990); *In re Esco Mfg. Co.*, 50 F.3d 315, 316 (5th Cir. 1995) (citation omitted).

Plan termination is a topic that Congress has addressed in painstaking detail in ERISA. *See* ERISA Sections 4041-48, 29 U.S.C. §§ 1341-48 (1994). The key termination provision in this highly detailed regulatory scheme reads:

> (1) Exclusive means of plan termination
>
> Except in the case of a termination for which proceedings are otherwise instituted by the [Pension Benefit Guaranty C]orporation as provided in section 4042 of this title, a single-employer plan may be terminated only in a

standard termination under subsection (b) of this section or a distress termination under subsection (c) of this section.

ERISA Section 4041(a)(1), 29 U.S.C. § 1341(a)(1)(1994).

Ignoring all but section 4044 of the statutory scheme, and relying on (1) a *superseded* tax regulation,[7] *see* Pet'r App. 11a n.3, and (2) an aberrant district court decision from the Fifth Circuit (which in turn relied on common law trust principles), *see id.* at 9a, the court of appeals held that Hughes may have "in effect, terminated" the plan or that its conduct may have amounted to a "constructive termination" of the plan, *see id.* at 10a, 11a n.3. As the court of appeals saw it, whether amending a retirement plan to add a new benefit formula amounts to "constructive" termination is a factual issue to be resolved only after discovery. *See id.* at 11a n.3, 22a-23a.

Yet there is nothing in the complaint or in the court of appeals' opinion to suggest that the Hughes amendment was any different from the type of plan amendment that thousands of employers routinely have adopted to alter, and typically to improve, plan benefits for participants. There appears to be

[7] *Compare* 26 C.F.R. § 1.411(d)-2(c) *with* 26 C.F.R. § 1.401-6(b)(1); *see also* Rev. Rul. 89-87, 1989-2 C.B. 81. The court of appeals' reliance on the tax-law concept of a "partial termination" is likewise badly mistaken. Events or developments that will amount to a termination or a "partial termination" for tax law purposes do not by themselves constitute or require a termination for purposes of ERISA. *See, e.g.*, ERISA Section 4043(c)(4), 29 U.S.C. § 1343(c)(4) (1994); *Chiles v. Ceridian Corp.*, 95 F.3d 1505, 1516 (10th Cir. 1996); *Chait* v. *Bernstein*, 835 F.2d 1017, 1020-21 (3d Cir. 1987); *United Steelworkers of America v. Harris & Sons Steel Co.*, 706 F.2d 1289, 1299 (3d Cir. 1983); *Baum v. Nolan*, 853 F.2d 1071, 1076-77 (2d Cir. 1988), *cert. denied*, 489 U.S. 1053 (1989).

no dispute that many active employees elected to continue making contributions in order to qualify for the older and more generous benefit formula. There are only conclusory allegations that "in effect" two plans were created and that the amendment was "equivalent" to a termination. Such allegations are simply artful pleading tactics designed to mask as a factual issue what in reality is a legal claim.

Employers commonly improve pension benefits for their employees by adding a separate benefit formula to the plan. In many cases, benefits are calculated separately for each employee under the several formulas in the plan, with the employee receiving benefits under the formula that produces the greatest benefit for that individual. But it is also a common practice, as was done here, to extend to new or future employees only the newly adopted benefit formula. If employers must run the risk on a case-by-case basis of having a court find as a factual matter that adoption of a new benefit formula somehow terminates a plan, possibly with very serious adverse tax consequences for both the employer and its employees, a very substantial and quite unnecessary obstacle will be placed in the path of improved employee benefits.

The court of appeals' suggestion that when a plan amendment limits a pre-existing benefit formula to current participants and applies a new formula to future participants, the amendment may amount to a "constructive termination" of the plan, *see* Pet'r App. 11a n.3, has very troubling implications that extend well beyond the immediate context of contributory defined-benefit plans. The notion that "freezing" or limiting an existing benefit formula to current participants is a "constructive" termination could mean, for example, that the Pension Benefit Guaranty Corporation would be required to assume many billions of dollars in additional termination liabilities for underfunded plans. *Cf. United Steelworkers of America v. Harris & Sons Steel Co.*, 706 F.2d 1289 (3d Cir.

1983). These uncertainties and potential serious consequences for plan beneficiaries, employers and the public generally are the result of the court of appeals' disregarding the specifics of the statutory scheme and "borrowing" from tax and from common law concepts to find support for its holdings.

This Court repeatedly has cautioned that "[t]he authority of the courts to develop a 'federal common law' under ERISA . . . is not the authority to revise the text of the statute," and that, particularly in the context of a very detailed and highly complex statute such as ERISA, "vague notions of a statute's 'basic purpose' are . . . inadequate to overcome the words of its text. . . ." *Mertens v. Hewitt Assoc.*, 508 U.S. 248, 259, 261 (1993), *aff'g* 948 F.2d 607 (9th Cir. 1991); *see also Rodriguez v. United States*, 480 U.S. 522, 525-26 (1987).

Unfortunately, by its reliance on just such vague notions, the court of appeals has reached a result that can only produce great confusion and uncertainty unless and until it is overturned.

CONCLUSION

For the foregoing reasons, ERIC urges the Court to grant the Petition for Writ of Certiorari.

Respectfully submitted,

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